

STATE OF MICHIGAN  
IN THE SUPREME COURT OF MICHIGAN

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NATIONAL WINE & SPIRITS, INC.,  
NWS MICHIGAN, INC., and  
NATIONAL WINE & SPIRITS, L.L.C.,

Plaintiffs-Appellants,

v

STATE OF MICHIGAN,

Defendant-Appellee,

and

MICHIGAN BEER & WINE WHOLESALERS  
ASSOCIATION,

Intervening Defendant-Appellee.

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Supreme Court Docket No.126121

Court of Appeals Docket No. 243524

Lower Court Case No. 02-13-CZ

**INTERVENING DEFENDANT-APPELLEE  
MICHIGAN BEER & WINE WHOLESALERS ASSOCIATION'S  
SUPPLEMENTAL BRIEF**

Respectfully submitted,

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BRIEF

## I. INTRODUCTION

By Order dated October 14, 2005, this Court has ordered oral argument on the Application for Leave and permitted the parties to supplement their briefing. The Application for Leave should be denied because it is futile. Any remedy NWS might seek is either in error under the recent US Supreme Court decision in *Granholm v Heald*, 544 U.S. \_\_\_\_ ; 125 S Ct 1885; 161 L Ed 2d 796 (2005) because it would interfere with the structure of wine and spirits distribution in Michigan under the unquestionably legitimate three tier system, or, is a self-defeating economic analysis. The claim of economic discrimination of out-of-state interests and protectionism of Michigan entities is belied by the right of NWS to enter Michigan as an ADA and the right of NWS to obtain licensure as a wine wholesaler. If NWS or any Michigan resident wanted to enter wine distribution, only, each would be treated the same. If NWS or any Michigan resident wanted to enter spirits distribution, each would be treated the same. Since NWS wants to be a combined spirits ADA and wine wholesaler, it again is treated the same; it just chose not to enter the Michigan wine market before 1999 as a wholesaler.

An unanswered question in the application for leave is what ultimate remedy does NWS seek? NWS fails to disclose what it seeks as an ultimate remedy. However, at the heart of NWS's Application is the economic theory that because of the \$7.48 per case state guaranteed payments to ADAs, there is a cost economy granted two other Michigan wine wholesalers/ADAs who NWS alleges control 70% of the wine distribution market<sup>1</sup>.

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<sup>1</sup> There is no competent, admissible evidence in the record that would support this point, since it is made only in an affidavit of "estimated" percentage, with no documented support. While Appellee does not accept that this is correct, and the claim that 70% of the wine market is controlled by two ADA/wholesalers is patently incorrect since TransCon is

If these allegations are true, wouldn't any Michigan business becoming either a wine wholesaler or an ADA for the first time have to cope with this? There is no discrimination.

**II. LEAVE TO APPEAL SHOULD BE DENIED FOR LACK OF A CLEAR AND COHERENT REMEDY SOUGHT.**

The Application does not make clear what remedy NWS is ultimately seeking. As a wholesaler of wine, is it to throw out the \$7.48 subsidy on spirits so that all non-ADA wine wholesalers are not subjected to an unequal state guaranteed reimbursement given to ADA spirits distributors? Or, does NWS (which reportedly now controls 52% of the spirits market in Michigan) seek to invalidate the public act that privatizes spirits distribution which contains the wine territory freeze for spirits distributors who also distribute wine? Or does NWS seek to disallow any wine wholesaler licensed in 1996 from being an ADA (with the result that NWS is the only spirits distributor with a monopoly on spirits distribution)<sup>2</sup>? Or, does NWS seek to pick and choose the parts of the Act it likes and dislikes and claim the benefits of being a subsidized spirits ADA (allowed to freely enter the State from Indiana), but then throw out the part with the wine territory limitation imposed on all spirits distributors who also distribute wine? Or, is NWS asking this Court to rewrite the statute -- a legislative prerogative -- so that there are no limitations for wine territories for ADAs?

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a joint venture made up of 3 wine wholesalers/ADAs, still for purposes of this brief NWS's position is accepted because it is self-defeating if correct. It shows that NWS, an out of state entity, was given *entre* into 30% of the wine markets with protection from other Michigan ADAs who could not use "combined cost economies" in those wine territories, to the benefit of NWS.

<sup>2</sup> Prior to passing the privatization legislation the legislature considered and rejected this approach.

Presumably it is the latter, but if so the implications of its position on economic discrimination are self-defeating. The NWS premise is that there is a “combined cost economies” factor of being both a subsidized spirits ADA and a wine wholesaler. (Application, p 12). As part of its construct, NWS alleges that there are two other ADA/wine wholesalers who control 70% of the wine market. (*Id*, footnote 7)

However, NWS fails to come to grips with the self-defeating nature of its argument on economic discrimination against out of state interests. If 70% of the wine market was controlled by Michigan wholesalers with ADA status, that means that in the 30% of the wine market where the wine territories were frozen in 1996 without a joint wine wholesaler/ADA, NWS as a newcomer from out of state who wanted to enter the Michigan market as a spirits distributor ADA was not only permitted to do so (belying discrimination), it was **protected** from having the other Michigan ADA/wine wholesalers who allegedly controlled 70% of the market from using their “combined cost economies” in the remaining 30% of the wine market. This belies any economic discrimination against out of state interests.

The other “fact” NWS proffers also reveals the self-defeating nature of its position. NWS asserts that the wines sold in Michigan today are 90% of the same wines sold in 1996. (Application p 11). However, that shows that new wines (in significant numbers) are constantly entering the market and NWS could enter the market as a wine wholesaler/ADA and bring new brands to market. NWS, like any Michigan entity, could also get wine territories by acquisition, purchase, or merger. MCL 436.1205(3).

NWS remains free to operate in Michigan and bring in new wine brands from Indiana and Illinois and any other state. There is no discrimination against out-of-state

**products.** There is no arguable “discrimination” against out-of-state businesses (with the possible exception of the wholesaler residency requirement, but that was not challenged in the trial court and is mooted by the absence of a timely challenge to it by NWS which is now a licensed wholesaler.)

**III. THE APPLICATION SHOULD BE DENIED BECAUSE NWS SEEKS A PROHIBITED OBJECT, IMPAIRING THE THREE TIER SYSTEM WITH PROBABLE VERTICAL INTEGRATION OF DISTRIBUTORS WITH MANUFACTURERS.**

The effect of striking part or all of the MCL 436.1205(3) must be considered in light of the 3 tier system. Again, the remedy is important. If NWS is granted relief, should the privatization of spirits legislation be stricken as invalid? Of course, NWS probably wouldn't want that but the privatization legislation should fall under NWS's *in pari materia* analysis. If, as relief, NWS wants no joint ADA/wholesalers and says the other 2 ADAs are disqualified since they were wholesalers in 1996, NWS would end up being the only spirits distributor, with a subsidized monopoly on spirits distribution in Michigan. If the wine territory restrictions on ADAs is thrown out as a remedy, there should be only 3 wine wholesalers, since with territory restrictions removed, NWS would join the other 2 ADAs in using “combined cost economies” to gobble up the rest of the wine territories and share all but a monopoly in controlling all the wine and all the spirits distribution in Michigan.

The reality is that what NWS is asking for would destabilize the 3 tier system of distribution of wine. It would leave a limited number of distributors, tending to near vertical integration with the manufacturers, *contra Traffic Jam & Snug, infra*, and disadvantage consumers by discouraging the bringing of new brands to market since the market would be sewn up with 3 main distributors, all with the “combined cost economies.” It cannot be

over stressed that this economic theory of NWS -- that “combined cost economies” are such a severe advantage/disadvantage to effectively discriminate -- means that if those “combined cost economies” are concentrated in 3 distributors (NWS, General, and Trans-Con) it must mean the economic demise of all other wine wholesalers who do not have guaranteed spirits payments.

NWS’s position strikes at the heart of the three tier system and is exactly contrary to two important cases. In *Granholm v Heald*, \_\_\_ US \_\_\_, 125 S Ct 1885, 1905; 161 L Ed 2d 796 (2005), the Supreme Court made clear that the structure of liquor distribution under a three tier system is unquestionably legitimate and within a state’s right to govern:

“The Twenty-First Amendment grants the States virtually complete control over whether to permit importation or sale of liquor **and how to structure the liquor distribution system.**” \*\*\*. States may also assume direct control of liquor distribution through state-run outlets **or funnel sales through the three-tier system.** We have previously recognized that **the three tier system is ‘unquestionably legitimate.’** (Emphasis added).

Of great importance, the instant case is about structure - whether to have wine territories frozen for combined ADA/wine distributors. **It is not about wine products** or any other product in interstate commerce being restricted from sale in Michigan in favor of a Michigan product. It is the goods themselves that are protected by the Commerce Clause. “Our Commerce Clause demands more than mere speculation to support discrimination against **out-of-state goods,**” *Id.*, 125 S Ct 1885, 1907. Here there are not out-of state goods involved as the victims of alleged discrimination. Rather only an out of state participant in the structure of distribution system who seeks to free itself from the structural limitations of being an ADA/wholesaler applied to all other in-state participants in the distribution structure. The wine itself is treated the same, and “State policies are

protected under the Twenty-first Amendment when they treat liquor produced out of state the same as its domestic equivalent.” *Id*, 125 S Ct 1885, 1905.

Thus, contrary to NWS’s attempts to lull the Court into a position of error, *Granholm v Heald* does not support NWS’s position but does support the position of Appellees. The structure of the three tier system is protected by the Twenty-first Amendment and is unaffected by the Commerce Clause where as here there is no interstate product affected in a discriminatory way.

With the unquestioned approval of the three tier system’s structural components by the U.S. Supreme Court, the second case of importance is *Traffic Jam & Snug, Inc v Liquor Control Commission*, 194 Mich App 640; 487 NW2d 768 (1992). It recognizes that the essence of the three tier system is preventing transfers of power between the tiers, and that a key provision of the Act, “proscribes several types of business arrangements that **tend to foster vertical integration**. Expressions of the Legislature’s intent to prevent vertical integration in the state’s liquor industry, and a few narrow exceptions for certain situations, may also be found elsewhere in the Liquor Control Act.” 194 Mich App 640, 643 (Emphasis added).

NWS thus seeks an impermissible object that militates against granting leave. It wants to eliminate wine territory restrictions on ADAs. However, the effect of doing so, according to NWS’s economic theory of “combined cost economies,” must be to tend to foster vertical integration by consolidating wine distribution into 3 distributors instead of at least 37, by cannibalizing the last 30% of the wine market by NWS and the other two ADA/wholesalers, leaving manufacturers with only having to deal with a limited number of

distributors. This will tend to foster vertical integration with manufacturers and limit brand development and distribution. In short, NWS presents a futile position, seeking in reality to gut the wine distribution structure in Michigan by eliminating all but three distributors (who would also control spirits), and eliminate all non-ADA wholesalers.

#### IV. CONCLUSION AND RELIEF REQUESTED

Not only does NWS's position on interstate discrimination make no sense when the economic realities of its premise are considered in light of the possible remedies, it makes no sense otherwise. The notion that there was active discrimination is laughable. How did it get to be an ADA if it is being discriminated against by the State of Michigan? Discriminatory intent is further belied by the admission that there were no out of state wholesalers at the time the wine territory legislation was adopted. The legislation was thus principally local and neutral, to stop Michigan wine wholesalers from being victimized by other Michigan wholesalers in a gold rush to grab territories or be consumed by ADAs.

Even if NWS is correct as to the market percentages, its position on discrimination is self-defeating: NWS was not only **not** discriminated against, it was allowed to enter Michigan and operate in 30% of the wine markets, **protected** from having any Michigan ADA/wholesalers operating there with "combined cost economies." There is no claim that NWS was challenging the wine wholesaler residency statute in 1996. It still doesn't challenge it, instead having chosen to become licensed as a wine wholesaler in 1999. NWS then filed this suit in 2002 seeking to cannibalize the remaining 30% of the wine market it used as a means of entry into Michigan as a spirits ADA.



There are no products being restricted from sale in Michigan so as to implicate commerce clause concerns. This suit is not about such commerce discrimination, but rather regulating the structure of wine distribution. NWS wants to have no wine territories so it can eliminate wine-only wholesalers and be one of only 3 ADA/wine wholesalers. It has at all time since ADAs were created in Michigan had the right to enter the Michigan market as an ADA. It had the right to become and, in fact, is a wine wholesaler. NWS has the right to bring new wine brands to market as a joint ADA/wine wholesaler and is not discriminated against in doing so. It has the right to acquire wine territories by acquisition, purchase, or merger, and is not discriminated against in doing so. It simply does not have the right to upset the structure of wine distribution after the ADA privatization. *Heald* makes clear that this is and remains a permissible area of regulation by the State.

For the foregoing reasons and those previously briefed in opposition to the application for leave, it should be denied.

Respectfully submitted,

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